Office - Supreme Court, U.S.
FILED
JAN 15 1982
ALEXANDER L. STEVAS,
CLERK

No. 81/1037

IN THE

# Supreme Court of the United States

October Term, 1981

ISRAEL AND RALEY,

*Petitioner,*

v.

FUTURONICS CORPORATION,

*Respondent.*

On Petition for a Writ of Certiorari To The
United States Court of Appeals for The Second Circuit

## BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

GARY L. BLUM
DANIEL A. ZIMMERMAN
FINLEY, KUMBLE, WAGNER,
HEINE, UNDERBERG & CASEY
425 Park Avenue
Telephone: (212) 371-5900
*Counsel for Respondent*

January, 1982

## QUESTIONS PRESENTED

The Petition raises no important questions for review by this court. It seeks only to sterilize Petitioner's egregious misconduct in flaunting and violating Bankruptcy Rules 215 and 219 and Petitioner's failure to comply with its fiduciary obligations to the bankruptcy court, by attempting to isolate and have this court view each violation and act of misconduct in a separate vacuum. It was, however, the totality of Petitioner's misconduct before the bankruptcy court that mandated the result below. The real questions presented here relate to factual issues and are two in number:

1. Whether where an attorney for a debtor-in- possession knowingly and willfully violates provisions of Bankruptcy Rules 215 and 219 by engaging in illicit fee-splitting and failing to disclose relationships with parties in interest, and over a period of four years secrets such violations from the court in breach of its fiduciary obligations to the court, such conduct is so egregious as to require a denial of all compensation to such attorney and render a grant of compensation to such attorney an abuse of discretion?

2. Assuming arguendo that Petitioner is entitled to some compensation despite the serious nature of its misconduct, whether the entry of the order retaining Petitioner as special counsel to the Debtor-in-Possession on a contingent fee basis, which order did not comply with the requirements of the applicable statutory provisions and rules and contained material misstatements and omissions, could be subsequently vacated, with counsel relegated to compensation on a quantum meruit basis?

The first question was answered in the affirmative by both the district court and the circuit court. The underlying findings of fact by the bankruptcy court have never seriously been questioned. Petitioner now seeks a further appellate review of what is essentially a factual determination peculiar to the facts of this case.

The second question was answered in the affirmative by both the bankruptcy court and the district court and not reached by the circuit court. (13a) It is also a question tied into the particular facts of the case and there is no showing of an abuse of discretion by the bankruptcy court in the initial ruling on this question. There is no need to address this question based upon the circuit court's ruling.

## TABLE OF CONTENTS


| | Page |
|---|---|
| QUESTIONS PRESENTED | (i) |
| TABLE OF AUTHORITIES | |
| Cases | (iv) |
| Statutes | (v) |
| Rules | (v) |
| Other Authorities | (v) |
| OPINIONS BELOW | 1 |
| JURISDICTION | 1 |
| STATUTES AND RULES INVOLVED | 2 |
| STATEMENT OF THE CASE | 2 |
| SUMMARY OF ARGUMENT | 7 |
| ARGUMENT | |
| POINT I: | |
| The Petition for Writ of Certiorari Was Not Timely Filed | 8 |
| POINT II: | |
| There Are "No Special and Important Reasons" for the Petition to be Granted | 11 |
| A. Introduction | 11 |
| B. The Petition Raises No Important Issues | 11 |
| C. There Exists No Conflict of Opinion Between the Decision Below and the Decisions of The Supreme Court or Other Circuit Courts | 12 |
| POINT III: | |
| The Circuit Court's Decision Affirming The District Court was Properly Decided and is Consistent with Clearly Defined Legal Principles | 15 |
| CONCLUSION | 19 |
| APPENDIX | |

## TABLE OF AUTHORITIES

*Cases:*


| | Page |
|---|---|
| *Arlan's Department Stores, Inc., In re,* 615 F.2d 925 (2d Cir. 1979) | 16, 17, 18 |
| *Baker* v. *Humphrey,* 101 U.S. 494 (1879) | 18 |
| *Barceloux, In re,* 74 F.2d 288 (9th Cir. 1934) | 13, 14 |
| *Bradford Electric Light Co.* v. *Clapper,* 284 U.S. 221 (1931) | 9 |
| *Citizens Bank of Michigan City* v. *Opperman,* 249 U.S. 448 (1919) | 9 |
| *Department of Banking* v. *Pink,* 317 U.S. 264 (1942), *reh. den.* 318 U.S. 802 (1943) | 10 |
| *Gypsy Oil Co.* v. *Escoe,* 275 U.S. 498 (1927) | 9 |
| *Haldeman Pipe & Supply Co., In re,* 417 F.2d 1302 (9th Cir. 1969) | 17 |
| *Layne & Bowler Corp.* v. *Western Well Works, Inc.,* 261 U.S. 387 (1923) | 11 |
| *Lucille's Inc., In re,* 26 F. Supp. 943 (D. Maine 1939) | 18 |
| *Mower* v. *Fletcher,* 114 U.S. 127 (1885) | 10 |
| *Ranchers Motor Inn, Inc., In re,* 527 F.2d 1044 (9th Cir. 1975) | 18 |
| *Rice* v. *Sioux City Cemetery,* 349 U.S. 70 (1954) | 11 |
| *Rogers Pyatt Shellac Co., In re,* 51 F.2d 988 (2d Cir. 1931) | 17 |
| *Ross* v. *Moffitt,* 417 U.S. 600 (1974) | 11 |
| *Rudolph* v. *United States,* 370 U.S. 269 (1962) | 12 |
| *Stolkin* v. *Nachman,* 472 F.2d 222 (7th Cir. 1974) | 13 |
| *Stratton, In re,* 51 F.2d 984 (2d Cir. 1931), *cert. den.* 76 L. Ed. 576 (1932) | 18 |
| *United States* v. *Johnson,* 268 U.S. 220 (1925) | 12 |
| *Watkins* v. *Sedberry,* 261 U.S. 571 (1923) | 14 |
| *Weil* v. *Neary,* 278 U.S. 160 (1929) | 16 |
| *Woods* v. *City Bank Co.,* 312 U.S. 262 (1941) | 18 |

| | Page |
|---|---|
| ***Statutes:*** | |
| Title 11, United States Code, Sec. 47(c) (1975) | 1 |
| Title 11, United States Code, Sec. 67(c) (1976) | 6 |
| Title 28, United States Code, Sec. 1254(a) | 1 |
| Title 28, United States Code, Sec. 2101(c) | 8 |
| ***Rules:*** | |
| Bankruptcy Rule 215 | i, 3, 5, 12, 13, 15, 17 |
| Bankruptcy Rule 219 | i, 3, 4, 5, 12, 15, 16, 17 |
| Federal Rules of Appellate Procedure, Rule 35(c) | 10 |
| General Order 44 | 13 |
| Supreme Court Rule 17.1 | 11 |
| Supreme Court Rule 20.2 | 8 |
| Supreme Court Rule 20.4 | 8, 9 |
| Supreme Court Rule 29 | 9 |
| ***Other Authorities:*** | |
| 3A Collier on Bankruptcy (14th ed.) ¶62.05 | 16, 18 |
| 3A Collier on Bankruptcy (14th ed.) ¶62.37 | 15, 16 |
| 12 Collier on Bankruptcy (14th ed.) ¶219.01 | 16 |
| Stern and Gressman, Supreme Court Practice (5th ed. 1978) | 9, 10 |

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1981

ISRAEL AND RALEY,

*Petitioner,*

v.

FUTURONICS CORPORATION,

*Respondent.*

# BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

## OPINIONS BELOW

The opinion and order of Bankruptcy Judge Stanley T. Lesser of the United States Bankruptcy Court for the Southern District of New York, dated September 28, 1979, appears in Petitioner's appendix (49a-76a) and is reported at 5 C.R.R. 871. The opinion and order of District Judge Kevin Thomas Duffy of the United States District Court for the Southern District of New York dated June 26, 1980 appears in Petitioner's appendix (26a-48a) and is reported at 5 B.R. 489. The majority and dissenting opinions of the United States Court of Appeals for the Second Circuit appear in Petitioner's appendix (3a-21a and 22a-25a respectively) and are reported at 655 F.2d 463. The order of the circuit court dated August 7, 1981 (filed September 4, 1981) denying Petitioner's petition for rehearing is not yet reported.

## JURISDICTION

Jurisdiction is invoked pursuant to former 11 U.S.C. §47c (1975) and 28 U.S.C. §1254(a). The order of the circuit court denying Petitioner's petition for rehearing is dated August 7, 1981. The petition for a writ of certiorari was filed on December 3, 1981 and was untimely.

## STATUTES AND RULES INVOLVED

The statutes and rules involved herein are set forth in an appendix annexed hereto.

## STATEMENT OF THE CASE

A Chapter XI petition and supporting documents were prepared by Arutt, Nachamie & Benjamin (the "Arutt firm") and filed on behalf of Futuronics Corporation ("Respondent" or "Debtor") on January 3, 1975. On that same day an order was entered retaining the Arutt firm under a general retainer in the Chapter XI case, as counsel for the Debtor.

The Arutt firm quickly discovered that Respondent's financial ill health was largely attributable to problems it had been experiencing with a series of government contracts. Lacking expertise in the field of government contract litigation, the Arutt firm decided that special counsel should be retained to represent Respondent in such matters.

On January 27, 1975, the Arutt firm met with Petitioner for the first time to discuss the possibility of the latter acting as special counsel to pursue Respondent's claims against the government. At that meeting, Petitioner agreed to share with the Arutt firm fees derived from its representation of Respondent; one third going to the Arutt firm, two thirds to be kept by Petitioner. This agreement was entered into despite Petitioner's knowledge that the Arutt firm had been retained to represent Respondent by prior order of the bankruptcy court. Neither the Arutt firm nor Petitioner knew at this meeting what legal services the Arutt firm would perform to earn the fee sharing in connection with the government litigation, and no procedure was set up for the two law firms to work together on Respondent's government contract litigation matters.

Petitioner was advised by the Arutt firm on January 27, 1975 that retention of counsel by a debtor-in-possession required an order of the bankruptcy court, and was also referred

to Bankruptcy Rule 219. Subsequently, the Arutt firm received an affidavit from Petitioner signed by Fred W. Israel, dated February 4, 1975 (the "February affidavit") to be utilized for the retention of Petitioner. Paragraph "10" of the February affidavit set forth the one-third two-thirds fee sharing arrangement between the two law firms.

The Arutt firm prepared an application to the bankruptcy court dated March 7, 1975, signed by the Arutt firm rather than by the Debtor as required by Bankruptcy Rule 215(a), and submitted it to the bankruptcy court with the February affidavit and a proposed retention order. The application and order were rejected by the bankruptcy court because of the fee-sharing arrangement between the two law firms. Petitioner then calculated that if the February affidavit were revised to omit all reference to any proposed fee sharing, it would be approved by the bankruptcy court. Accordingly, a "replacement affidavit" was submitted by Petitioner to the Arutt firm with former paragraph "10" deleted. The original fee sharing agreement between the two firms, however, was not terminated.

When Petitioner's retention order was entered on March 10, 1975 (the "Retention Order"), the bankruptcy court had no reason to believe that any agreement existed between Petitioner and the Arutt firm, nor that any division of fees would occur, nor that any relationship between the two law firms existed other than that both law firms were retained in separate orders to represent Respondent. Nothing contained in the Retention Order, application and affidavit alerted the bankruptcy court to the fact that Petitioner planned to violate the Bankruptcy Rules by sharing its fees without court approval. Petitioner's misrepresentation was compounded by the misstatement in the application that "no prior application" had been made for the requested retention, though both law firms knew that a prior application had been submitted to and rejected by the bankruptcy court because of the fee sharing arrangement set forth in the February affidavit.

For a period of four (4) years, Petitioner and the Arutt firm secreted their relationship from the bankruptcy court. The two law firms never came to the bankruptcy court at any time to inform it of the alleged working relationship or for a determination of how fees should be distributed between them. Petitioner paid the Arutt firm only after it had first received more than sufficient funds from the Debtor to cover the payments. From March 3, 1975 to January 28, 1977, Petitioner was paid a total of $179,247.65 by Respondent in six payments. From May 13, 1976 to May 18, 1977, Petitioner paid the Arutt firm, pursuant to invoices submitted by the latter to the former, a total of $60,066.59, 33.5% of the funds received by Petitioner from Respondent.

Arutt firm time records and original entries to substantiate invoices to Petitioner were destroyed prior to the hearings before the bankruptcy court and the bankruptcy court could not verify time allegedly expended. The services allegedly performed by the Arutt firm for which Petitioner presumably made payment were either of a non-legal nature or non-existent, or of such minimal consequence as to be "cosmetic", both law firms closing their eyes to the nature of the billings, or lack of services. The fee sharing arrangement was nothing more than a "bald fee-splitting agreement... accepted by the Israel firm with full knowledge of its implications notwithstanding the cosmetic references to services and assistance to be contributed by the Arutt Firm." (58a)

Petitioner negotiated a settlement stipulation in January 1979 with the government on behalf of Respondent. Shortly after approval of the settlement, Petitioner submitted proposed orders seeking to have the bankruptcy court fix its compensation in accordance with the contingent fee schedule incorporated by reference in the Retention Order. Judge Lesser refused to sign such orders and instead directed Petitioner to seek allowances for compensation in a manner consistent with Bankruptcy Rule 219. In an affidavit sworn to on April 9, 1979, Petitioner presented a detailed "Statement Of Services Ren-

dered By Special Counsel." The affidavit disclosed for the first time that Petitioner had paid the Arutt firm approximately $60,000 in fees in connection with the government contract litigation. Upon this disclosure, Respondent moved that all compensation to the Arutt firm and to Petitioner be denied based upon the apparent violations of law.

After a full hearing, Judge Lesser determined that any work performed by the Arutt firm with respect to the government contract litigation had been done without court approval and thus in direct violation of Rule 215(a). (64a) Furthermore, Judge Lesser noted that the proposed order submitted in March 1975 for the appointment of the Israel firm as special counsel "did not contain the affirmation of Blanck as president of Futuronics" (62a); "did not reveal the connections between the Israel and Arutt firms" (62a); and falsely stated that "no prior application for the relief sought" had been made (62a). Judge Lesser discovered in the course of the hearings that contrary to the statement contained in the application for the Retention Order, a prior application had indeed been presented to and rejected by Judge Herzog in February, 1975. Judge Lesser discovered that after Judge Herzog had rejected the initial application, another was submitted which deleted the objectionable language concerning fee sharing. The bankruptcy judge determined that the parties decided nevertheless to maintain their fee-sharing arrangement as evidenced by a letter dated March 3, 1975, without disclosing the agreement to the court. Thus, Judge Lesser concluded that Judge Herzog had signed the Retention Order without knowledge of the underlying agreement that had been entered into between the Arutt and Israel firms.

Judge Lesser also concluded that the the record revealed that the Arutt firm and Petitioner had entered into an illicit fee-sharing arrangement in violation of Bankruptcy Rule 219(d). He noted his authority to withhold compensation entirely but chose to limit the sanctions against the firms.

The parties appealed to the district court pursuant to §39(c) of the former Bankruptcy Act, 11 U.S.C. §67(c)(1976). Judge Duffy affirmed the bankruptcy court's decision to the extent of its findings of misconduct and rejection of the contingent fee compensation provisions, but reversed insofar as the order granted either of the firms any compensation. He determined that the bankruptcy court had abused its discretion in allowing any fees to the law firms in view of the serious nature of the attorneys' misconduct. (48a)

Judge Duffy noted that Petitioner and the Arutt firm had engaged in "a fee splitting arrangement in flagrant disregard of the Bankruptcy Rules" (46a); had "intentionally kept the bankruptcy court in the dark about [the] arrangement for four years despite the numerous opportunities" to disclose the agreement (46a); and had only revealed the illicit agreement after the court had requested a statement of services (46a). He opined that had the bankruptcy court not requested the statement of services and had instead deferred to the contingency fee provisions contained in the Retention Order, "the parties would never [have] revealed the fee splitting arrangement." (46a) Judge Duffy additionally noted that "once faced with this serious situation, both firms pled ignorance of the Bankruptcy Rules and attempted to place the blame" upon the Debtor. Judge Duffy decided that the record belied the law firms' contentions of ignorance (46a).

The district court concluded that the conduct of the two law firms "was totally unprofessional and in breach of their respective duties as fiduciaries and officers of the court." Judge Duffy stated that "the conduct of both firms evinces 'a total pattern of conduct which betrays a callous disregard of the professional obligations undertaken in... a bankruptcy [proceeding].'" (47a) The district court concluded that under the circumstances of the case, "a Judge would indeed be remiss if he were to permit a law firm guilty of such conduct to be compensated." (47a)

The circuit court affirmed the decision of the district court, holding that:

> "Whatever discretion a bankruptcy court judge may have to fashion an appropriate sanction for an attorney's violation of the bankruptcy rules and breaches of his fiduciary obligations to the court, given the egregiousness of the conduct here, it was an abuse of that discretion to permit the appellants to retain any of the fees they had received, let alone to allow any further compensation." (20a-21a)

Petitioner then sought rehearing before the Second Circuit, which motion was denied by order dated August 7, 1981, precipitating the instant petition for a writ of certiorari.

## SUMMARY OF ARGUMENT

I. The petition for a writ of certiorari must be dismissed as untimely because it was filed more than 90 days after the date of the circuit court's denial of Petitioner's petition for rehearing.

II. There are "no special and important reasons" for the petition for writ of certiorari to be granted because the decisions below are limited to the facts of the case and there is no conflict between the circuits on the governing legal principles.

III. Based upon the findings of fact by the bankruptcy court, the decisions of the circuit court and the district court are proper and correct.

## ARGUMENT

### POINT I
### THE PETITION FOR WRIT OF CERTIORARI WAS NOT TIMELY FILED

In an opinion and order dated August 7, 1981 (1a), the circuit court denied Petitioner's petition for rehearing. The opinion and order were not filed by the clerk of the circuit court until September 4, 1981 (2a), at which time the clerk noted that a suggestion for rehearing en banc had been transmitted to the judges of the court in regular active service and to any other judge on the panel that heard the appeal and that no such judge requested that a vote be taken thereon (77a-78a). The instant petition was filed on December 3, 1981, exactly ninety (90) days after the opinion and order below were filed, but one hundred and fourteen (114) days from the date of the denial of rehearing.

The time within which a petition for writ of certiorari may be filed is governed by 28 U.S.C. §2101(c) [see Supreme Court Rule 20.2] which provides in pertinent part:

> "Any other appeal or any writ of certiorari intended to bring any judgment or decree in a civil action, suit or proceeding before the Supreme Court for review shall be taken or applied for within ninety days after the entry of such judgment or decree."

Where, however, the petition for writ of certiorari follows a petition for rehearing below, this rule is somewhat modified. Supreme Court Rule 20.4 provides:

> " . . . If a petition for rehearing is timely filed by any party in the case, the time for filing the petition for writ of certiorari for all parties (whether or not they requested rehearing or joined in the petition for rehearing) runs from the date of the denial of rehearing or of the entry of a subsequent judgment entered on the rehearing."

Therefore, where, as in the instant case, there is denial of rehearing, a petition for writ of certiorari must be brought

within ninety (90) days of such denial. Since the period for applying for a writ of certiorari has not been extended [see Supreme Court Rule 29], Petitioner was required to serve and file its petition for writ of certiorari within ninety (90) days of August 7, 1981, the date of the denial of its petition for rehearing—i.e., by November 5, 1981. This it failed to do. A petition for writ of certiorari which is not timely filed must be denied. *Bradford Electric Light Co.* v. *Clapper,* 284 U.S. 221 (1931).

It is readily apparent that in a case such as the one at bar, the operative date with respect to the commencement of the time within which to file a petition for writ of certiorari is the date of the order denying rehearing and not the date the order was filed. The wording of Supreme Court Rule 20.4—"the date of denial of rehearing or the entry of a subsequent judgment" creates a clear distinction between the date of an order and the date of filing or entry of the order, the latter being applicable only where the petition for rehearing results in a new judgment. Where, as in this case, rehearing is denied, the date of filing of the denial order is irrelevant.

The computation of the ninety (90) day period from the date of denial of rehearing, and not from the date of filing, has long been the practice of this Court. As stated in *Citizens Bank of Michigan City* v. *Opperman,* 249 U.S. 448, 450 (1919):

> Where a petition for rehearing is entertained, the judgment does not become final for purposes of our review until such petition has been denied or otherwise disposed of, and the three months' limitation begins to run from date of such denial or other disposition."

*Accord, Gypsy Oil Co.* v. *Escoe,* 275 U.S. 498 (1927).

A leading treatise on Supreme Court practice describes the underlying rationale:

> "If a rehearing is sought in the court below, there is no absolute certainty that the judgment below will not be altered. Only when there is such certainty can the judg-

> ment properly be made the subject of a petition for certiorari. And thus it is that the time for petitioning for certiorari commences on the date when certainty and finality attach to the action taken by the lower court. Where rehearing has been sought, that date is the one on which rehearing was denied." Stern and Gressman, Supreme Court Practice, at 399 (5th ed. 1978).

When the petition for rehearing was denied by opinion and order dated August 7, 1981, "certainty and finality" attached to the action taken by the circuit court. The subsequent filing by the clerk of the circuit court is thus of no moment. As stated in *Department of Banking* v. *Pink*, 317 U.S. 264, 267 (1942) *reh. den.* 318 U.S. 802 (1943):

> "[A]... judgment [is]... final and reviewable when it ended the litigation by fully determining the rights of the parties, so that nothing remained to be done by the lower court except the ministerial act of entering the judgment which the appellate court had directed:" (citing *Mower* v. *Fletcher*, 114 U.S. 127 (1885)).

That a suggestion for rehearing *en banc* had been made did not, of course, affect the finality of the August 7 order.

> "The pendency of such a suggestion whether or not included in a petition for rehearing shall not affect the finality of the judgment of the court of appeals or stay the issuance of the mandate." Federal Rules of Appellate Procedure, Rule 35(c).

The suggestion for rehearing *en banc* thus did not affect the operative date from which the time to petition for certiorari began to run, which is the date of denial of rehearing.

It is respectfully submitted that since the petition for writ of certiorari was served and filed on December 3, 1981, in excess of ninety (90) days from August 7, 1981, the date of denial of the petition for rehearing, such petition was not timely. The petition should therefore be denied and dismissed as untimely.

## POINT II

## THERE ARE "NO SPECIAL AND IMPORTANT REASONS" FOR THE PETITION TO BE GRANTED

### A. Introduction

The Supreme Court's decision to grant or deny a petition for certiorari "is discretionary and depends on numerous factors other than the perceived correctness of the judgment [the court is] asked to review." *Ross* v. *Moffitt,* 417 U.S. 600, 617 (1974). "A review on writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only when there are special and important reasons therefor." Supreme Court Rule 17.1.

"[I]t is very important that [the Supreme Court] be consistent in not granting the writ of certiorari except in cases involving principles the settlement of which is of importance to the public as distinguished from that of the parties, and in cases where there is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal." *Rice* v. *Sioux City Cemetery,* 349 U.S. 70, 79 (1954) (citing *Layne & Bowler Corp.* v. *Western Well Works, Inc.,* 261 U.S. 387, 393). The instant petition creates no important issues nor does it point to any conflict between the circuits. Although it is Respondent's position that the judgment of the court of appeals below was in all respects correct (see Respondent's Point III), even were this not the case, the instant petition raises no "special and important reasons" for its granting, and should therefore be denied.

### B. The Petition Raises No Important Issues

The only real issues Petitioner raises in its petition turn on the particular facts of this case alone. Did Petitioner enter into a bald fee-splitting agreement? Did Petitioner conceal such agreement from the bankruptcy Court for four years? Did Petitioner do so with full knowledge that it was thereby violating the Bankruptcy Rules and breaching its fiduciary duty to the bankruptcy court? These are the only questions pertinent to a review of this case, and they have twice been answered in

the affirmative by appellate courts. In essence, therefore, Petitioner is asking this Court to make a third review of the lengthy record to see if it can alter the conclusions two previous appellate courts have reached. Such fact canvassing is not a task to be served by a grant of certiorari. "We do not grant a certiorari to review evidence and discuss specific facts." *United States* v. *Johnson,* 268 U.S. 220, 227 (1925).

In the words of the court of appeals below, "given the egregiousness of the conduct here, it was an abuse of [the bankruptcy court's] discretion to permit the appellants to retain any of the fees they had received, let alone any further compensation." (20a-21a) It is Petitioner's conduct which is at the heart of this case: conduct so extreme as to merit severe sanctions. A review of these facts "would be of no importance save to the litigants themselves." *Rudolph* v. *United States,* 370 U.S. 269, 271 (1962). Certiorari should therefore be denied.

**C. There Exists No Conflict of Opinion Between the Decision Below and the Decisions of The Supreme Court or Other Circuit Courts**

Sanctions imposed against attorneys for their misconduct relate to the nature and extent of the evil committed. When such misconduct is viewed as a broad continuum ranging from the minor to the extreme, it is clear that Petitioner's actions fall at the extreme end of the spectrum. Cases cited by Petitioner involve acts of misconduct far less obnoxious than those committed here, and in no event does Petitioner refer to a decision which holds that an attorney who violates the disclosure provisions of Bankruptcy Rule 215, the fee-splitting prohibition of Bankruptcy Rule 219, and who breaches the fiduciary duty owed to the bankruptcy court by each attorney, is entitled to any compensation.

Typical of the authority relied upon by Petitioner in support of its assertion that the decision below conflicts with the

decision of this court and the circuit courts is *Stolkin* v. *Nachman*, 472 F.2d 222 (7th Cir. 1974), which Petitioner argues, involves "a substantially similar factual record to the instant case" (Petition at 30). In that case, the attorney for the debtor filed a bankruptcy petition under the imminent pressure of foreclosure proceedings and in his precipitous haste, neglected to obtain a retention order. Upon the completion of the bankruptcy proceedings, the debtor refused to compensate his attorney and the matter was litigated before the bankruptcy court and then reviewed by the district court. The case then came before the Seventh Circuit where the debtor raised the issue of the failure to obtain a retention order for the *first time*. The court disposed of the debtor's contention on the ground that "any error not presented below will be lost on appeal", but stated that had the question been raised below, it "would indeed be a serious one." *Id.*, 472 F.2d at 226.

In apparent *dicta*, the *Stolkin* court argued that compensation should be awarded to the attorney since "[t]here is no hint that if the petition required by General Order No. 44 (superceded by Bankruptcy Rule 215) had been prepared it would have been subject to any challenge." *Id.* This was of course not true in the instant case where Petitioner's initial petition for retention was rejected by the bankruptcy court because of its reference to the illegal fee splitting agreement, and its second petition was granted only because the firm fraudulently concealed its unlawful intentions. While *Stolkin*, at best, excuses an attorney's technical oversight, the instant case involves an attorneys calculated misrepresentation. The two cases stand at opposite ends of the misconduct continuum and as such they do not conflict.

Neither does *In re Barceloux*, 74 F.2d 288 (9th Cir. 1934) conflict with the decision below. In that case, the attorneys of record for the trustee, Devlin & Devlin, associated themselves with an attorney who provided them with "legal assistance." This attorney had a large personal claim against the estate, a fact which he failed to disclose to the bankruptcy court. The

circuit court allowed reasonable compensation to Devlin & Devlin only, and not to the "associate attorney", despite the former's request for "fees and compensation" on behalf of the latter. *Id.* 74 F.2d at 294. The court further held that Devlin & Devlin's association with the "associate attorney" did not taint its representation or operate against the magnitude of its fee since the attorney did not violate any rule of the court and his representation was "open". *Id.*, at 295. The instant case, as contrasted with *Barceloux,* involves the willful concealment of material information by special counsel in flagrant violation of the bankruptcy rules. *Barceloux* thus offers no conflict.

Similarly, petitioners argue that the decision below conflicts with *Watkins* v. *Sedberry,* 261 U.S. 571 (1923) in which this court granted compensation to an attorney who had entered into a champertous agreement. In *Watkins,* the court noted that the severity of the champerty rule had been relaxed and that in fact champerty was not prohibited under state law. However, because no state court decision had sustained a champertous contract, the court instead allowed recovery by the attorney in *quantum meruit.* The *Watkins* court was clearly not troubled by the ethical implications of the attorneys conduct in that case, a situation markedly different from the "egregious conduct" found by the courts below.

The remaining decisions cited by Petitioner are likewise of no moment, for none of them discuss the extreme level of attorney misconduct found in the instant case. At best, the cases referred to by Petitioner support the proposition that an attorney may at times neglect to follow the letter of the law and still be worthy of compensation from his client. This proposition hardly conflicts with the decision below which holds that a willful violation of the law by an attorney and a subsequent concealment of such violation from the court, requires the most severe of sanctions.

## POINT III

## THE CIRCUIT COURT'S DECISION AFFIRMING THE DISTRICT COURT WAS PROPERLY DECIDED AND IS CONSISTENT WITH CLEARLY DEFINED LEGAL PRINCIPLES

The decision of the circuit court that a denial of compensation to Petitioner was warranted and required by Petitioner's violations of Bankruptcy Rules 215 and 219 and breaches of Petitioner's fiduciary obligations to the bankruptcy court is based upon long-standing and well-settled law on this issue. The outcome of the bankruptcy proceeding is immaterial. "It is the *potential* danger alone that makes them obnoxious." 3A Collier on Bankruptcy (14th ed.) ¶62.37 at 1636. (Emphasis in original).

In affirming the district court's reversal of the bankruptcy court on the compensation issue, the circuit court held:

> "Whatever discretion a bankruptcy court judge may have to fashion an appropriate sanction for an attorneys violation of the bankruptcy rules and breaches of his fiduciary obligation to the court, given the egregiousness of the conduct here, it was an abuse of that discretion to permit [the Israel] firm to retain any of the fees they had received, let alone to allow any further compensation." (20a-21a)

More particularly, the circuit court stated the following in relation to Petitioner's conduct during these bankruptcy proceedings: (1) it "betrays a callous disregard of the professional obligations undertaken" (20a); (2) "the appointment of the Israel firm was calculated to deceive" (18a); (3) they "deviously deleted the unseemly portions from their application" (18a); (4) they "covertly agreed to maintain" their illicit fee-splitting agreement (18a); (5) "their lack of fidelity was manifested time and time again before the court" (19a); (6) "we find outrageous, the Israel firm's failure to disclose" (19a);

(7) "the Israel firm cavalierly professed ignorance of the bankruptcy rules." (19a)

From these findings the circuit court affirmed both the bankruptcy court and the district court in holding that Petitioner's conduct was a clear violation of Bankruptcy Rules 219(a) and (d). The Court emphasized that Petitioner's "violations of subdivision (a) and (d) of Rule 219 provide an *independent basis* for denying compensation." (17a) (Emphasis added).

The statutory prohibition against fee-splitting embodied in Bankruptcy Rule 219(d) emanates from this court's decision in *Weil* v. *Neary,* 278 U.S. 160, 173 (1929), which held that arrangements not approved by the court for the division of compensation are contrary to public policy not only because of "actual evil results but their tendency to evil in other cases." The basis for the underlying prohibition against such arrangement is that it results in a clear transfer of judicial power over expenditures and allowances from the Court to others. 3A Collier on Bankruptcy (14th ed.), ¶62.37, pg. 1637. See also 12 Collier on Bankruptcy (14th ed. 1975) ¶219.01, *et seq.*, stating that "any division of fees or other compensation represents, above all, an incentive for the applicant to claim a compensation high enough to make his own share in it a worthwhile remuneration. It thereby tends towards extravagance of expenditure. . . ."

While Bankruptcy Rule 219(d) does not make it mandatory for the bankruptcy court to deny all compensation, where blatant violations of said Rule have been committed, as in the instant case, it is clear that imposition of such a result is appropriate. See *In re Arlan's Department Stores, Inc.,* 615 F.2d 925 (2d Cir. 1979); 3A Collier on Bankruptcy, ¶62.05. Petitioner knowingly intended to deceive the bankruptcy court concerning the illicit fee-splitting arrangement. Petitioner secreted its unauthorized payments to the Arutt firm until April, 1979 when the bankruptcy court demanded full disclosure. Even then, Petitioner attempted to disguise the agreement as a law firm subcontracting agreement although legal services were

not provided to Petitioner by the Arutt firm, as invoices with unsupported time recapitulations were sent and received to document the alleged services. Payment of sums in excess of $60,000, constituting approximately one-third of the fees paid to Petitioner by Respondent were paid to the Arutt firm in direct violation of Bankruptcy Rule 219(d). As stated by Bankruptcy Judge Lesser, "the two-third one-third arrangement was a bald fee-splitting agreement . . . accepted by the Israel firm with full knowledge of its implications." (58a)

Petitioner also clearly violated Rule 215 as the bankruptcy court was not informed of the retention agreement with the Arutt firm until four years after the entry of the order approving the Israel firm's retention. As stated by the circuit court:

> "From the beginning a cloud hung over the appointment of the Israel firm. Rule 215 expressly required the Israel firm to disclose all 'connections' it had with the attorneys for the debtor. This it failed to do." (15a)

It is well settled that attorneys, particularly in a bankruptcy situation, have a clear and unequivocal duty to reveal all connections with the bankrupt, the creditors or any other parties in interest, and their respective attorneys. *In re Haldeman Pipe & Supply Co.,* 417 F.2d 1302 (9th Cir. 1969). As stated in *In re Rogers Pyatt Shellac Co.,* 51 F.2d 988, 992 (2d Cir. 1931):

> "Attorneys who seek appointment . . . owe the duty of complete disclosure of all facts bearing upon their eligibility for such appointment. If that duty is neglected, however innocently, surely they should stand no better than if it had been performed... If the rule is to have vitality and the evils against which it is aimed are to be eliminated, it should be enforced literally."

The duty of counsel for the debtor in a bankruptcy proceeding to disclose fully to the court all connections that may exist between counsel and the debtor, arises not solely by reason of the bankruptcy rules, but also is founded upon "the

fiduciary obligation owed by counsel for the debtor to the bankruptcy court." *In re Arlans Department Store, Inc, supra,* 615 F.2d at 937. See also, *Woods* v. *City Bank Co.,* 312 U.S. 262, 269 (1941). At bar, the circuit court held that Petitioner "flagrantly breached" its fiduciary obligations to the bankruptcy court. (18a) The court emphasized:

> "This is not a case of technical noncompliance as the parties would have us characterize their conduct; rather as Judge Lesser determined below, '[t]he entire process pertaining to the March 11, 1975 order either was calculated to deceive Judge Herzog or was rife with deficiencies which undercut its very existence.'" (18a)

It is incontrovertible that the bankruptcy court may deny fees and disbursements in a bankruptcy proceeding where serious breaches of fiduciary obligations occur. See, *In re Arlans Department Store, Inc., supra; In re Ranchers Motor Inn, Inc.,* 527 F.2d 1044 (9th Cir. 1975); *In re Lucille's, Inc.,* 26 F. Supp. 943 (D. Maine 1939); 3A Collier on Bankruptcy *supra,* at ¶62.05. *Accord, In re Stratton,* 51 F.2d 984 (2d Cir. 1931), *cert. den.* 76 L. Ed. 576 (1932). The professional obligations which Petitioner and all attorneys assume can be summarized from the opinion of this Court in *Baker* v. *Humphrey,* 101 U.S. 494, 502 (1879), recently cited with approval in *In re Arlans Department Store, Inc., supra:*

> "They are officers of the law, as well as the agents of those by whom they are employed. Their fidelity is guaranteed by the highest considerations of honor and good faith and to these is superadded the sanction of an oath. The slightest divergence from recitude involves the breach of these obligations. None are more honored or more deserving than those of the brotherhood who, uniting ability with integrity, prove faithful to their trusts and worthy of the confidence reposed in them. Courts of justice can best serve both the public and the profession by applying firmly upon all proper occasions the salutary rules which have been established for their governments in doing business with their clients."

In light of Petitioner's unjustifiable conduct, it is patently clear that the ruling of the circuit court was in all respects proper. This case "is not one of isolated instances of oversight, but involves a total pattern of conduct which betrays a callous disregard of the professional obligations undertaken in the bankruptcy proceedings." (20a) Petitioner's attempt to make a major issue of judicial or public concern ripe for consideration by this court out of what is no more than the application of well settled legal principles to an insidious pattern of professional misconduct must fail.

## CONCLUSION

Respondent respectfully submits that the Petition should be denied.

Dated: January 11, 1982

Respectfully submitted,

GARY L. BLUM
DANIEL A. ZIMMERMAN
FINLEY, KUMBLE, WAGNER,
HEINE, UNDERBERG & CASEY
425 Park Avenue
New York, New York 10022
(212) 371-5900
*Counsel for Respondent*

## APPENDIX

## STATUTES AND RULES INVOLVED

28 U.S.C. §2101(c)

(c) Any other appeal or any writ of certiorari intended to bring any judgment or decree in a civil action, suit or proceeding before the Supreme Court for review shall be taken or applied for within ninety days after the entry of such judgment or decree. A justice of the Supreme Court, for good cause shown, may extend the time for applying for a writ of certiorari for a period not exceeding sixty days.

Supreme Court Rule 17.1

**CONSIDERATIONS GOVERNING REVIEW ON CERTIORARI**

1. A review on writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only when there are special and important reasons therefor. The following, while neither controlling nor fully measuring the Court's discretion, indicate the character of reasons that will be considered.

(a) When a federal court of appeals has rendered a decision in conflict with the decision of another federal court of appeals on the same matter; or has decided a federal question in a way in conflict with a state court of last resort; or has so far departed from the accepted and usual course of judicial proceedings, or so far sanctioned such a departure by a lower court, as to call for an exercise of this Court's power of supervision.

(b) When a state court of last resort has decided a federal question in a way in conflict with the decision of another state court of last resort or a federal court of appeals.

(c) When a state court or a federal court of appeals has decided an important question of federal law which

has not been, but should be, settled by this Court, or has decided a federal question in a way in conflict with applicable decisions of this Court.

Supreme Court Rules 20.2 and 20.4

**REVIEW ON CERTIORARI TIME FOR PETITIONING**

* * *

2. A petition for writ of certiorari in all other cases shall be deemed in time when it is filed with the Clerk within the time prescribed by law. See 28 U.S.C. §2101(c).

* * *

4. The time for filing a petition for writ of certiorari runs from the date the judgment or decree sought to be reviewed is rendered, and not from the date of the issuance of the mandate (or its equivalent under local practice). However, if a petition for rehearing is timely filed by any party in the case, the time for filing the petition for writ of certiorari for all parties (whether or not they requested rehearing or joined in the petition for rehearing) runs from the date of the denial of rehearing or of the entry of a subsequent judgment entered on the rehearing.

Bankruptcy Rules 215(a) and (b)

**EMPLOYMENT OF ATTORNEYS AND ACCOUNTANTS**

(a) *Conditions of Employment of Attorneys and Accountants.* No attorney or accountant for the trustee or receiver shall be employed except upon order of the court. The order shall be made only upon application of the trustee or receiver, stating the specific facts showing the necessity of such employment, the name of the attorney or accountant, the reasons for his selection, the professional services he is to render, and to the best of the applicant's knowledge all of the attorney's or accountant's connections with the bankrupt, the creditors, or any other party in interest, and their respective attorneys and accountants. If

the attorney or accountant represents or holds no interest adverse to the estate in the matters upon which he is to be engaged, and his employment is in the best interest of the estate, the court may authorize his employment. Notwithstanding the foregoing sentence, the court may authorize the employment of an attorney or accountant who has been employed by the bankrupt when such employment is in the best interest of the estate. The employment of any attorney or accountant shall be only for the purposes specified in the order, but the court may authorize a general retainer of an attorney when necessity therefor is shown.

(b) *Employment of Attorney or Accountant with Adverse Interest.* If without disclosure any attorney or accountant employed by the trustee or receiver shall represent or hold, or shall have represented or held, any interest adverse to the estate in any matter upon which he is so employed, the court may deny the allowance of any compensation to such attorney or accountant, or the reimbursement of his expenses, or both, and may also deny any allowance to the trustee or receiver if it shall appear that he failed to make diligent inquiry into the connections of such attorney or accountant.

Bankruptcy Rules 219(a), (b) and (d)

## COMPENSATION FOR SERVICES RENDERED AND REIMBURSEMENT OF EXPENSES INCURRED IN A BANKRUPTCY CASE

(a) *Application for Compensation or Reimbursement.* A person seeking compensation for services, or reimbursement of necessary expenses, from the estate shall file with the court an application setting forth a detailed statement of (1) the services rendered and expenses incurred, and (2) the amounts requested. An application for compensation shall include a statement by the applicant as to what payments have theretofore been made or promised to him for services rendered or to be rendered in any capacity whatsoever in connection with the case, the source of the compensation so paid or promised, whether any compensation he has previously received has been

shared and whether an agreement or understanding exists between the applicant and any other person for the sharing of compensation received or to be received for services rendered in or in connection with the case, and the particulars of any such sharing of compensation or agreement or understanding therefor, except that the details of any agreement by the applicant for the sharing of his compensation as a member or regular associate of a firm of lawyers or accountants shall not be required. The requirements for this subdivision shall apply to an application for compensation for services rendered by an attorney or accountant even though the application is filed by a creditor or other person on his behalf.

(b) *Disclosure of Compensation Paid or Promised to Attorney for Bankrupt.* Every attorney for a bankrupt, whether or not he applies for compensation, shall file with the court on or before the first date set for the first meeting of creditors, or at such other time as the court may direct, a statement setting forth the compensation paid or promised him for the services rendered or to be rendered in connection with the case, the source of the compensation so paid or promised, and whether the attorney has shared or agreed to share such compensation with any other person. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of his compensation with a member or regular associate of his law firm shall not be required.

* * *

(d) *Restriction on Sharing of Compensation.* Except as herein provided, a person rendering services in a bankruptcy case or in connection with such a case shall not in any form or guise share or agree to share the compensation paid or allowed him from the estate for such services with any other person, nor shall he share or agree to share in the compensation of any other person rendering services in a case under the Act or in connection with such a case. This rule does not prohibit an attorney or accountant from sharing his compensation as

trustee, receiver, attorney, or accountant with a member or regular associate of his firm, or from sharing the compensation received by his firm or by any other member or regular associate thereof, and does not prohibit an attorney from sharing in the compensation received by his firm or by any other member or regular associate thereof, and does not prohibit an attorney for a bankrupt or for a petitioning creditor from sharing his compensation for services rendered with any other attorney contributing thereto. If a person violates this subdivision, the court may deny him compensation, may hold invalid any transaction subject to examination under Rule 220 to which he is a party, or may enter such other order as may be appropriate.